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SUBJECT: REGULATORY OFFICIAL REJECTS BUNDESBANK-BAFIN MERGER RUMORS

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¶1. (U) Summary: A senior financial regulator at BaFin in Bonn recently confirmed to us that plans to merge BaFin with the Bundesbank have been dropped. He predicted that more Landesbanken would merge, leading ultimately to only two or three such banks nationally. He commented that WestLB, the troubled state Landesbank for North Rhine-Westphalia, is in better shape than its reputation, in part because its new CEO has introduced more transparency in its operations. End Summary.

Rejects Rumor of Bundesbank-BaFin Merger

¶2. (U) A senior BaFin official confirmed to Pol/Econoff recently that its merger with the Bundesbank, rumored for months, would not occur. The Bundesbank does not want to lose its independence, which would occur if it were to take over BaFin's regulatory functions, and he doubted that the Bundesbank was interested in insurance regulation, one of BaFin's three regulatory roles (the others cover banks and stocks). Asserting that the division of labor between the two institutions is working well, he added that ongoing efforts to develop a unified EU-wide banking supervision system made a merger impractical because EU standards were not yet set. He also stated that Bundesbank President Axel Weber, who he speculated has the best chance to replace Trichet as ECB head, would push for EU standards after he takes over. In any case, a Deutsche Bank official reminded Frankfurt Pol/Econoff, a merger would require federal legislation, which is unlikely in view of the Bundestag elections in September.

WestLB and the NY Fed

¶3. (U) On the crisis at WestLB, the state-owned Landesbank for North-Rhine Westphalia, the BaFin official noted that the change in CEO has brought much needed transparency. For example, there is now such a close working relationship between the NY Fed and WestLB that a Fed official works in the WestLB New York office, with access to all internal communications and systems. He suggested that if the State Department or Treasury wish to know more about WestLB's U.S. operations, which he considers important and rather successful, the NY Fed has better access than even BaFin.

The Future of the Landesbanks

¶4. (U) Regarding the future of the German Landesbank system, the BaFin official predicted that only two or three of the Landesbanks will survive the current financial crisis, citing Bavaria and Rhineland-Pfalz as examples. He raised the possibility that one of the Landesbanks could fuse with DEKA, the umbrella bank jointly held by the savings banks (Sparkassen) and the Landesbanks, but declined to elaborate.

Comment

¶5. (SBU) This is the most authoritative statement we have heard that the rumored merger between BaFin and the Bundesbank will not take place. Our BaFin interlocutor, however, may be biased in favor of Germany's current banking supervision model, as he was BaFin's chief negotiator in talks with the Bundesbank that led to the division of labor between the two institutions. The very close cooperation between WestLB and the NY Fed reflects the new WestLB leadership's strategy of moving quickly to fix its many problems.

¶6. (U) This message was coordinated with Embassy Berlin and ConGen Frankfurt.

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